

JAN 9 2006

RECEIVED  
FEDERAL ELECTION  
COMMISSION  
SECRETARIAT

2005 JAN -9 A 10:10

**BEFORE THE FEDERAL ELECTION COMMISSION**

In the Matter of )

Community Water System, Inc. )

Gill Elrod Ragon Owen & Sherman P.A. )

Charles McLaughlin )

Cora McLaughlin )

Charles C. Owen )

Luke Quinn )

Heartsill Ragon III )

Danny Roberson )

Greg Smith )

Sharon Smith )

Chris Travis )

MUR 5514

**SENSITIVE**

**GENERAL COUNSEL'S REPORT #2**

**I. ACTIONS RECOMMENDED**

Take no further action with respect to any of the respondents and close the file.

**II. BACKGROUND**

This matter was generated by a referral from the State of Arkansas Contractors Licensing Board. Information contained in the referral indicated that Community Water System, Inc. ("CWS"), an Arkansas non-profit domestic corporation, through the activities of former CWS General Manager Greg Smith, might have reimbursed political contributions made by outside vendors of CWS to the campaigns of Senator Tim Hutchinson and Representative Marion Berry. The referral in this matter, and the information available at the reason to believe stage, rested primarily on a December 3, 2002 memorandum written by CWS employee Shelly Davis, who was Greg Smith's personal secretary, and accompanying corroborative documents. See MUR 5514, First General Counsel's Report dated August 5, 2004 ("FGCR") at 3-9. The Commission made reason to believe findings with respect to CWS, Greg Smith, his wife Sharon, Gill Elrod

1 Ragon Owen & Sherman P.A. ("the Gill Law Firm") and three of its attorneys, Charles  
2 McLaughlin and his wife Cora, and two other CWS vendors, Danny Roberson and Luke Quinn,  
3 for contributions made in 2002, and authorized an investigation.

4  
5  
6  
7  
8  
9  
10 As discussed below, while we do not rule out that there may have been a corporate  
11 reimbursement scheme, we recommend that the Commission take no further action against any  
12 of the respondents and close the file in this matter.

### 13 III. ANALYSIS

#### 14 A. The Gill Law Firm and its Attorneys

15 The Federal Election Campaign Act of 1971, as amended (the "Act") prohibits  
16 corporations from making contributions or expenditures from their general treasury funds in  
17 connection with a federal election. *See* 2 U.S.C. § 441b(a). The Act also provides that no person  
18 shall make a contribution in the name of another person or knowingly permit his or her name to  
19 be used to effect such a contribution, and that no person shall knowingly accept a contribution  
20 made by one person in the name of another person. *See* 2 U.S.C. § 441f. This prohibition  
21 extends to persons who knowingly help or assist in making such contributions. *See* 11 C.F.R.  
22 § 110.4(b)(1)(iii).

1 At the reason to believe stage, it appeared for several reasons that CWS might have  
2 reimbursed three Gill Law Firm attorneys, Heartsill Ragon III, Charles C. Owen and Chris  
3 Travis, for their 2002 political contributions to Senator Hutchinson and Representative Marion  
4 Berry, totaling \$4,000. The whistleblower, Shelly Davis, stated in her memorandum that Greg  
5 Smith had instructed Ragon in July 2002 to submit \$2,000 invoices in both July and August  
6 2002. Thereafter, the Gill Law Firm submitted July and August 2002 invoices to CWS, each  
7 with a \$2,000 "miscellaneous reimbursements" entry, totaling \$4,000. According to Davis, Greg  
8 Smith rejected these invoices, and told Ragon to reword the terminology "miscellaneous  
9 reimbursements" to something he had written on a piece of paper. The invoices were then  
10 revised to state that the fees were for "series of intraoffice conference re: various long-term  
11 planning, finance and operational issues."<sup>1</sup>

12 We were also in possession of an October 7, 2002 email exchange between Davis and  
13 Ragon, in which Davis specifically referred to two invoices "that were for Berry's campaign  
14 contribution and Hutchinson's contribution." Ragon responded to Davis' email without  
15 commenting on her characterization of the two invoices. *See* FGCR at 8. Moreover, CWS  
16 effectively acknowledged the existence of a reimbursement scheme when it cited Smith's  
17 activities on behalf of CWS involving illegal contributions to political candidates as one of the  
18 bases upon which they terminated him.<sup>2</sup> The Gill Law Firm returned \$4,000 to CWS in  
19 November 2002, and CWS terminated its relationship with that firm in early 2003.

---

<sup>1</sup> Both CWS and the Gill Law Firm were unable to provide a copy of the original August 2002 Gill Law Firm invoice. However, in his interview, Smith confirmed that the original August 29, 2002 invoice also included a \$2,000 "miscellaneous reimbursements" charge.

<sup>2</sup> CWS also noted in response to the Commission's reason to believe findings that it is currently involved in two lawsuits with Greg Smith. In one of these two lawsuits, Greg Smith claims that CWS wrongfully terminated his employment. CWS Resp at 4

1 As discussed below, while this Office has developed evidence sufficient to meet the  
2 probable cause standard that CWS reimbursed the Gill Law Firm, the investigation was unable to  
3 establish that the Gill Law Firm reimbursed any of the three attorneys.

4 The three attorneys each confirmed in interviews that they made contributions to either or  
5 both Marion Berry for Congress and Tim Hutchinson for Senate in August 2002,<sup>3</sup> but each  
6 denied participating in a reimbursement scheme. Chris Travis, a first time political contributor,  
7 told us that Ragon solicited him to make his \$1,000 contribution.

8 In our interview with Shelly Davis, who is still employed by CWS, she reiterated that in  
9 2002, she overheard a telephone conversation between Smith and Ragon relating to the July and  
10 August 2002 invoices and the reimbursement of political contributions. Specifically, Davis told  
11 us that on July 15, 2002, Smith, using his speakerphone, instructed Ragon to submit a \$2,000  
12 invoice in both July and August to cover the expense of making contributions to Representative  
13 Marion Berry and Senator Tim Hutchinson, and she provided what she says are her  
14 contemporaneous notes of this conversation.<sup>4</sup> Shortly thereafter, she saw a \$2,000  
15 "miscellaneous reimbursements" entry in each of the Gill Law Firm's July and August 2002  
16 invoices.

17 Davis also reiterated that on September 25, 2002, she was present when Smith directed  
18 Ragon to change the "miscellaneous reimbursements" entries on the July and August 2002  
19 invoices to something he had written on a piece of paper. Moreover, she elaborated on this part

---

<sup>3</sup> Ragon is reported as contributing \$1,000 each to the Berry (received 8/12/02) and Hutchinson (received 8/30/02) committees; Travis is reported as contributing \$1,000 to the Berry committee (received 8/12/02) and Owen is reported as contributing \$1,000 to the Hutchinson committee (received 8/30/02).

<sup>4</sup> Shelly Davis stated that she sat in an adjoining office to Greg Smith's office, separated by a sliding door that was usually kept open, permitting her to hear Greg Smith's telephone conversations, frequently conducted by speakerphone. In his interview with this Office, Smith acknowledged that he often used his speakerphone and that Davis sat in the adjoining office—facts that were also confirmed by Leslie Smith, former CWS comptroller.

1 of her account. After the September 25<sup>th</sup> board meeting, she stated, Smith accused Ragon of  
2 overcharging, but Ragon reminded Smith that they had increased the amount of the invoice to  
3 cover \$2,000 in contributions to Berry and Hutchinson. According to Davis, Smith  
4 acknowledged, "Yeah, you're right." Davis also testified to this effect under oath in legal  
5 proceedings between CWS and Greg Smith. Although Greg Smith in his interview with us  
6 denied that he directed Ragon to amend the invoices to better conceal political contribution  
7 reimbursements, he confirmed to us that Davis was present when he returned the invoices to  
8 Ragon and told him that the Gill Law Firm's miscellaneous charges were unacceptable, thus  
9 placing Davis in a position to hear the conversation between Smith and Ragon.

10 Further, Ragon's explanations for the "miscellaneous reimbursements" entries are  
11 contradicted by both Smith and by Charles Owen, president of the Gill Law Firm. In his  
12 interview, Ragon stated that during the summer of 2002, several problems developed concerning  
13 the CWS project the law firm was working on, and it appeared that a proposed bond issue might  
14 not succeed. He stated that this uncertainty, coupled with concerns over unbilled time, caused  
15 the Gill Law Firm to consider terminating its representation of CWS unless a solution could be  
16 developed. Therefore, according to Ragon, CWS, through Greg Smith, orally agreed with Ragon  
17 to pay the Gill Law Firm an arbitrary figure of \$2,000 per month until the bond issue problems  
18 were resolved.

19 Greg Smith, however, denied in his interview that there was any such oral arrangement.  
20 Although he acknowledged that funding for the CWS project was in jeopardy between July and  
21 September 2002, Smith told us that the Gill Law Firm never mentioned the possibility of  
22 dropping CWS as a client during that period or any other time. Moreover, Smith stated that there  
23 was never an understanding that the Gill Law Firm would bill CWS an additional \$2,000 in July

1 and August as a means of compensating the law firm in the event that the bond issue did not  
2 pass. Smith also denied that he and Ragon orally agreed that the \$2,000 "miscellaneous entries"  
3 on the 2002 July and August invoices at issue would represent payment for unbilled activity.  
4 Owen also contradicted Ragon. Owen could not recall any occasion on which the firm had  
5 contemplated terminating its representation of CWS, which at the time was one of the Gill Law  
6 Firm's biggest clients. Considering all of the testimony together, we find Davis' account of the  
7 interaction regarding the "miscellaneous reimbursements" the most credible.

8 In her interview, Davis told us that after informing some of the CWS Board members of  
9 the alleged reimbursement scheme, she sought to provide additional documentation.

10 Accordingly, she sent the October 7, 2002 email to Heartsill Ragon that specifically referenced  
11 the returned Gill Law Firm invoices for political contributions to Representative Berry and  
12 Senator Hutchinson, and asked that Ragon fax to her attention the revised invoices; Ragon  
13 replied by email that he would do so. In his interview, Ragon stated that he did not remember the  
14 email exchange, but does not deny that that he had received and replied to Davis' email; his only  
15 explanation was that he did not read it carefully. This explanation is questionable given the  
16 relatively short length of the email and the prominence of the language concerning the  
17 contributions. In addition, one would expect an attorney to pay some attention to detail when  
18 reading and responding to communications from a client.

19 During our investigation, we also interviewed Pete Gist, who is currently president of the  
20 CWS board and was a CWS board member in 2002. He told us that after Davis informed him  
21 and other CWS Board members of the alleged reimbursement scheme, he confronted Greg  
22 Smith. Gist says he asked Smith if CWS had ever made political contributions, and Smith

1 replied that it had; Gist asked how much, and, Gist asserts, Smith said \$20,000.<sup>5</sup> Greg Smith  
2 confirmed in his interview that when Gist asked him for a yes or no answer whether  
3 professionals were reimbursed for political contributions through CWS funds, Smith said "yes."  
4 Smith, however, claims that he then explained to Gist that CWS paid the professional people  
5 working on its project, and the professional people made their own contributions from the money  
6 they earned. Smith said that he believes that Gist did not fully understand what he was trying to  
7 tell him, and denied that he admitted to Gist that CWS funds were used to reimburse individuals  
8 for political contributions.<sup>6</sup> However, Smith's explanation appears to be a contorted and  
9 confusing response to what was a straightforward question.

10 Finally, Richard Mays, an attorney retained by three CWS Board members to investigate  
11 Shelly Davis' allegations, also concluded that Smith and Ragon agreed to participate in a  
12 corporate reimbursement scheme. In an affidavit (and later in interviews), Mays described, in  
13 very specific terms, a face-to-face meeting on December 13, 2002 with Ragon and his law  
14 partner, John Gill, at which Mays asserts both admitted to Ragon's participation in the alleged  
15 reimbursement scheme. *See Attachment 1.* Mays' account draws support from Greg Smith's  
16 former advisor Joseph Marshall's interview statement that Mays told him on December 15, 2002  
17 that he had obtained such admissions.<sup>7</sup> Greg Smith acknowledged in his interview that Marshall

---

<sup>5</sup> Gist brought this statement to the attention of Barbara Sullivan, who then stated to the press that she expected the full scope of the reimbursement scheme to reach at least \$20,000 in reimbursed contributions. As noted elsewhere in this report, we have been unable to confirm reimbursed contributions in that amount.

<sup>6</sup> Smith told the same story under oath in a July 2003 hearing before the Arkansas Employment Security Department during his unsuccessful attempt to prove his eligibility for unemployment compensation benefits after CWS terminated his employment.

<sup>7</sup> Marshall is an attorney who at the time was admitted to practice law in Minnesota but had recently moved to Arkansas and was not yet admitted there. He was apparently informally advising Smith in connection with Smith's impending termination by CWS

1 transmitted this information to him.<sup>8</sup>

2 Thus, Davis has presented a consistent account, corroborated by documentary and  
3 testimonial evidence, that there was a corporate reimbursement scheme involving Greg Smith  
4 and the Gill Law Firm. In contrast, on a key issue, Smith did not support Ragon's explanation of  
5 the circumstances leading to the \$2,000 invoices in July and August 2002. Moreover, Ragon's  
6 explanation of his failure to contradict Davis' email appears less than credible. Finally, there is  
7 the indisputable fact that the Gill Law Firm returned \$4,000 to CWS after allegations surfaced.  
8 However, we were not able to establish through documentary evidence that after CWS paid the  
9 Gill Law Firm \$4,000, the firm reimbursed the attorneys for their political contributions.

10  
11  
12  
13  
14  
15 According to the Gill Law Firm, shareholders (as opposed to associates) do not  
16 receive a salary, but instead are paid draws during the year at their request. The "paydraw"  
17 process, as described by the Gill Law Firm, is related to a productivity formula and allows each  
18 shareholder within the firm to orally request a "paydraw" check, which is issued by the office  
19 administrator. Shareholders can make such a request at any time, and are not required to

<sup>8</sup> Mays and others also told us that on Sunday evening, December 15, 2002, he participated in a conference call arranged by Marshall that also included Greg Smith, Heartsill Ragon and John Gill. During that phone call, Ragon and Gill denied making the admissions alleged by Mays. See Attachment 1 at pages 4-5. Likewise, in our interviews with Ragon and Gill, each denied ever making such admissions to Mays.



1 complete a form or specify the work involved for the draw request.<sup>9</sup> The three Gill Law Firm  
2 attorneys who made the political contributions in issue were shareholders during October 2002,  
3 the month that CWS paid the Gill Law Firm for the July and August 2002 invoices totaling  
4 \$4,000. In accordance with the process, none of the three attorneys specified in writing the  
5 purpose of any of their respective "paydraws," and there were no paydraws neatly corresponding  
6 in terms of timing and amount to the contributions in issue. Further, the Gill Law Firm's  
7 expense reimbursement documents, which consisted of copies of reimbursement checks, receipts  
8 and reimbursement request forms, were not facially suspicious and did not correlate in amount to  
9 the contribution that each respective attorney made to recipient committees; most of the expenses  
10 were for dining and travel and were under \$200. Thus, we do not possess sufficient documentary  
11 evidence to prove that the Gill Law Firm reimbursed the attorneys for their political  
12 contributions. Of course, if there had been a reimbursement scheme, since CWS paid the  
13 invoices in issue in October 2002, and the Gill Law Firm returned the \$4,000 to CWS in  
14 November 2002, it is possible that the planned reimbursements, if any, never took place.

15 Without evidence that CWS's funds, rather than the individual contributors' funds, were  
16 used to make the contributions attributed to them, we cannot establish violations of 2 U.S.C.  
17 §§ 441b and 441f. A section 441f violation occurs if a person writes a contribution check after  
18 having been paid by some other person for that contribution, or if they are later reimbursed for  
19 the contribution. Conversely, if the Gill Law attorneys who wrote the checks to the recipient

---

<sup>9</sup> The "paydraws" received throughout the year are compared with the shareholder's production output. If the shareholder's productivity exceeds his/her draws, he or she is paid the difference at the end of the year, if the shareholder generates a negative balance, then he or she owes the firm the balance. Shareholders received no bonuses that were separate from having a positive balance at the end of the year. On December 31, 2002, all three of the respondent attorneys received lump sum amounts far exceeding the amounts of their respective 2002 contributions.

1 committees were not using, or were not reimbursed by, someone else's money, then they actually  
2 made the contributions from their own funds, and no one made a contribution in the name of  
3 another. Therefore, in the absence of evidence showing that any of the Gill Law Firm attorneys  
4 were reimbursed for making their respective contributions, we cannot prove that such  
5 reimbursements took place. While we could likely establish that there was an attempt to make  
6 contributions in the names of others, the Act does not prohibit possible unsuccessful attempts to  
7 violate it.

8 This Office does not believe that the relatively small amount in violation warrants the  
9 additional expenditure of the Commission's resources in attempting to substantiate that CWS,  
10 through the Gill Law Firm, reimbursed the firm's attorneys for political contributions. Therefore,  
11 we recommend that the Commission take no further action against the Gill Law Firm  
12 respondents.

13 B. Other CWS Vendors, Cora McLaughlin, and Sharon Smith

14 Three persons whose businesses were CWS vendors—Charles McLaughlin, Luke Quinn  
15 and Danny Roberson—plus Charles McLaughlin's wife, Cora, and Greg Smith's wife, Sharon,  
16 also contributed to the Hutchinson and Berry campaigns in 2002. Shelly Davis' memorandum,  
17 other documentation, and the timing of the contributions indicated that CWS might have  
18 reimbursed these individuals for their contributions, FGCR at 14-15, and the Commission  
19 accordingly made reason to believe findings. During our investigation, each of these individuals  
20 submitted affidavits denying they participated in the alleged reimbursement scheme.<sup>10</sup> See  
21 Attachments 2-6. Further, CWS informed us that it was unable to detect any suspicious billing

<sup>10</sup> In a September 13, 2004 letter to the Office of the General Counsel, Sharon Smith states that she adopts all statements and arguments made by Greg Smith in his response to the Commission's reason to believe findings, including the enclosed affidavit. See Attachment 4 at 1, 6, and 7.

1 on the part of Charles McLaughlin's, Luke Quinn's, and Danny Roberson's respective  
2 companies, and has continued its business relationships with these respondents.

3 Likewise, we were unable to isolate possible reimbursements in these respondents'  
4 companies' billings to CWS. We examined the invoices submitted by those vendors to CWS.  
5 They appear to be for the sorts of goods and services ordinarily provided to CWS and are for  
6 relatively large amounts, as compared to the contributions, during the relevant time period. For  
7 example, Mr. and Mrs. McLaughlin made a total of \$4,000 in political contributions to the Berry  
8 and Hutchinson campaigns in August and September 2002, but McLaughlin's company,  
9 McLaughlin Engineering, received payments from CWS for invoices submitted during that time  
10 period in the amounts of \$18,675, \$30,450, \$22,007, \$18,175, and \$30,450. Nor were we able to  
11 identify any possible reimbursements to Greg Smith or his wife, of Sharon Smith's two \$1,000  
12 contributions in 2002 through CWS's payments to Greg Smith.<sup>11</sup>

13 Although it is possible to disguise reimbursements of the relatively small amounts of  
14 these contributions in such large figures, in the absence of anyone admitting to the scheme, we  
15 cannot detect from the face of the invoices where such reimbursements, if they exist, would be  
16 hidden. Further, the small amount of the alleged conduits' contributions, which collectively  
17 totaled \$9,000 during 2002, does not appear to justify the use of more resources—such as the  
18 deposing of the vendors' bookkeepers or other personnel—to pursue possible violations by them.  
19 Given our inability to trace reimbursements from CWS to the other CWS vendors, Sharon Smith,  
20 and Cora McLaughlin, and given their affidavits denying any involvement in a reimbursement

---

<sup>11</sup> In his interview with this Office, Greg Smith said that Sharon Smith's contributions came from a joint account. Sharon Smith, who was present during the phone interview of her husband, commented that she could only recall attending one of the three fundraisers that reportedly received contributions from her.

1 scheme, we recommend that the Commission take no further action and close the file with  
2 respect to these respondents.

3 With respect to Greg Smith, the FEC contributor database shows that he did not make any  
4 reported Federal contributions in 2002. Therefore, his potential liability in this matter would  
5 arise through his approval as a corporate officer of reimbursements for contributions made by  
6 others. For the reasons discussed with respect to the other respondents, we also recommend that  
7 the Commission take no further action with respect to him.

8 We make the same recommendation as to CWS. Even if we could have traced the  
9 reimbursements to the contributors, based on everything else we know now, we likely would  
10 have recommended the Commission take no further action against CWS. CWS cooperated with  
11 the investigation. It appears that no one at high levels at the company, other than Greg Smith,  
12 had knowledge of the alleged reimbursement scheme. The CWS Board members apparently first  
13 learned of the alleged reimbursement scheme from Davis in the fall of 2002. CWS terminated its  
14 relationships with both Greg Smith and the Gill Law Firm shortly thereafter; it continued its  
15 relationships with the other vendors only when it could not find evidence of false billings.

16

17

1

2

3

4

5

6

Based on the above, this Office recommends that the Commission take no further action against Community Water System, Inc., Greg Smith, Gill Elrod Ragon Owen & Sherman P.A., Heartsill Ragon III, Charles McLaughlin, Cora McLaughlin, Luke Quinn, Danny Roberson, Sharon Smith, Charles C. Owen and Chris Travis and close the file in MUR 5514.

7

8

9

10

11

12

#### IV. RECOMMENDATIONS

1. Take no further action against Community Water System, Inc., Greg Smith, Gill Elrod Ragon Owen & Sherman P.A., Heartsill Ragon III, Charles McLaughlin, Cora McLaughlin, Luke Quinn, Danny Roberson, Sharon Smith, Charles C. Owen, and Chris Travis.
2. Close the file.

3. Approve the appropriate letters.

Lawrence H. Norton  
General Counsel

Rhonda J. Vosdinh  
Associate General Counsel  
for Enforcement

12/20/05  
Date

BY:

Susan L. Lebeaux  
Susan L. Lebeaux  
Assistant General Counsel

Roy Q. Lockett  
Roy Q. Lockett  
Attorney

Attachments:

1. Richard Mays Affidavit
2. Charles McLaughlin Affidavit
3. Cora McLaughlin Affidavit
4. September 13, 2004 Letters with enclosed Greg Smith Affidavit
5. Luke Quinn Affidavit
6. Danny Roberson Affidavit